

STATE OF VERMONT
HUMAN SERVICES BOARD

In re)	Fair Hearing No. 9776
)	
Appeal of)	

INTRODUCTION

The petitioner appeals the decisions by the Department of Social Welfare terminating her household's Food Stamps and her children's Medicaid benefits. The issues are 1) whether depreciation is an allowable deduction from income for food stamp purposes and 2) whether the proceeds from the sale of livestock are income or resources under the Food Stamp and Medicaid programs.

FINDINGS OF FACT

The facts are not disputed. The petitioner is a farmer who from time to time buys and sells dairy cows. In April, 1990, the Department notified the petitioner that her food stamps were being closed and that Medicaid coverage for her children was being terminated because the family's income was too high.

The petitioner maintains that the Department should have allowed depreciation as a cost of producing self-employment income, and counted the proceeds from the sale of livestock as a resource rather than as income. The Department maintains that the applicable federal and state regulations dictate that depreciation is not an allowable deduction from self-

employment income, and that the sale of livestock must be considered self-employment income, not resources.

ORDER

The Department's decision regarding the treatment of proceeds from the sale of livestock as income to the petitioner is affirmed. The Department's decision disallowing a deduction from income for depreciation is reversed, and the matter is remanded to the Department to consider the petitioner's actual and specific depreciation costs.

REASONS

1) Sale of Livestock

A) Medicaid

Medicaid Manual (MM) § M342.3 provides as follows:

Income Producing Property

Personal property "used as a means a livelihood" (i.e., to produce income) is excluded from total value of combined resources.

Income producing property may include tools, livestock, equipment, machinery and similar goods owned, usually in quantities beyond the customary needs of normal living, and in fact, used by members of an assistance group to produce income for support of the group. This may include income producing property owned by a recipient who is currently unemployed, but can reasonably be expected to return to work. However, if there is no expectation that the recipient will return to work, at least in that particular field, then the personal property shall be considered as a resource.

Medicaid Manual § M344.1 provides:

Sale of real or personal property generally has the effect of converting an excluded asset to a liquid asset subject to the combined resources limitations.

The petitioner argues that the proceeds from the sale of livestock--an excluded resource--should continue to be considered a resource--albeit non-excluded--under the above section. However, this argument ignores the definition "earned income" contained in the regulations.

Medicaid Manual § M352 provides, in pertinent part (with emphasis added):

Earned income shall include all wages, salary, commissions or profit from activities in which the individual is engaged as an employee or a self-employed person, including but not limited to active management of capital investments (e.g., rental property).

Earned income is defined as income prior to any deductions for income taxes, FICA, insurance or any other deductions voluntary or involuntary except that, in determining earned income for self-employed individuals, business expenses are deducted first.

Earnings over a period of time, for which settlement is made at one given time, are also included; i.e., sale of farm crops, livestock, poultry, etc. . . .

Based on the wording of the above regulations, it seems beyond dispute that the Medicaid program considers livestock of farmers, who are engaged in the business of buying and selling livestock, to be a resource until they are sold--then, the profit from their sale is considered income. The Department's decision in this regard is affirmed.

B) Food Stamps

Food Stamp Manual (FSM) § 273.8(e)(5) includes in the definition of excludable resources, "property such as farm land or work related equipment, such as tools of a tradesman or the machinery of a farmer, which is essential to the employment or self-employment of a household member". The petitioner is correct that dairy cows used to produce farming income are covered by this definition.

Food Stamp Manual § 273.9(b) includes the following definition of income:

Household income shall mean all income from whatever source excluding only items specified in paragraph (c) of this section.

1. Earned income shall include:

- i All wages and salaries of an employee
- ii The gross income from a self-employment enterprise, including the total gain from the sale of any capital goods or equipment related to the business, excluding the costs of doing business as provided in paragraph (c) of this section. . .

The petitioner argues that even when she sells her livestock, the proceeds from the sale should remain considered as resources--not income. In support of this argument the petitioner cites O'Dea v Commissioner of Public Welfare, 437 NE 2d 540 (Mass. App., 1982), which held that when a gas-station owner was operating at a loss and began to sell inventory at a loss without replacement, such "withdrawals from inventory" were not income, but were available non-exempt resources for food stamp purposes. The key to this decision, however, is that the inventory was

sold at a loss, and thus did not produce income. id. p 542.

No similar claim is made by the petitioner herein. The food stamp regulations, like Medicaid (see supra), consider only the profit of the sale of goods or equipment to be income. Presumably, the petitioner was given ample opportunity to demonstrate whether or not she had a net gain from the sale of the livestock in question. Assuming there was some profit realized from the sale, there is no question that the amount of this profit was properly deemed to be "income" by the Department in the calculation of the petitioner's food stamps.

II) Depreciation (food stamps)

As noted above, the food stamp regulations define as earned income from self-employment "total gain. . . excluding the costs of doing business as provided by paragraph (c) of this section." § 273.9(b)(1)(ii). Food Stamp Manual § 273.9(c)(9) lists as excluded income: "The cost of producing self-employment. The procedures for computing the cost of producing self-employment income are described in 273.11."

Food Stamp Manual § 273.11(a)(4) includes the following provisions:

Allowable Costs Of Producing Self-Employment Income

- i Allowable costs of producing self-employment income include, but are not limited to, the identifiable costs of labor, stock, raw material, seed and

fertilizer, interest paid to purchase income-producing property, insurance premium, and taxes paid on income-producing property.

- ii In deterring net self-employment income, the following items shall not be allowable as a cost of doing business.

. . .

D. Depreciation.

The Department maintains that the above provision plainly and simply precludes consideration of depreciation as an allowable cost (or exclusion) of producing self-employment income. The petitioner argues that the above provision conflicts with the federal statute and with Congressional intent in enacting the federal statute.

7 U.S.C. § 2014(d)(9) includes in the definition of income, ". . . all income from whatever source excluding only . . . the cost of producing self-employment income. . . ." The statute makes no specific mention of "depreciation" as a cost of producing income.

In amending the food stamp statutes in 1977, Congressional Committees wrestled with the problems of accurately and fairly computing self-employment income. House Conference Report No. 95-599, 95th Con., 1st Sess. 24, Reprinted in 1977 U.S. Code Cong. and Ad. News at P. 2014-2015 contains the following discussion:

Cost of producing self-employed income.--All Federal benefit programs exclude this cost in ascertaining income for eligibility purposes.

The Department's instructions currently include--

"Net adjusted income from self-employment, which will be the total gross income from such enterprise (including the total gain received from the sale of any capital goods or equipment related to such enterprise) less the cost of producing that income."

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In the regulations, however, the Department has stated that costs of producing income from self-employment are all costs except:

- (1) Payments on the principal of the purchase cost of income producing real estate. Any payments of principal, interest, and taxes on the home shall be subject to paragraph (c)(1)(iii)(h) of this section;
- (2) Payments on the principal of the purchase cost of capital assets, equipment, machinery, and other goods;
- (3) Depreciation; and
- (4) A net loss sustained in any previous period. . .

While the accelerated forms of depreciation afforded under the Internal Revenue Code as a matter of legislative grace would not necessarily constitute costs of doing business and producing income, some factor for wear and tear of machinery and buildings, obsolescence and accrued replacement costs should be inherent in doing business.

Thus, the Department would be expected to revise its regulations in this regard to allow some form of depreciation in arriving at the cost of producing income by a self-employed individual, although that should be administratively simplified by the use of simple schedules covering entire categories of equipment rather than separate rates for each item.

. . .

Thirteen years have passed since the 1977 amendments and the federal agency has not removed the depreciation disallowance contained in 7 C.F.R. § 273.11(a)(4). It seems

clear, however, that in enacting 7 U.S.C. § 2014(d)(9) (supra) Congress did intend to include depreciation as a legitimate and quantifiable (i.e., "inherent") cost producing self-employment income. To the extent that the federal regulation conflicts with this intent, it cannot be construed as an outright and total prohibition on the consideration of depreciation as a cost of producing self-employment income. In light of the legislative history of the federal statute (supra), the regulation can be reconciled with the statute only by considering "depreciation" in § 273.11(a)(4)(ii)(D) as the IRS method of calculating depreciation, which the Congressional Committee acknowledged "would not necessarily constitute costs of doing business and producing income". It cannot, however, be construed as disallowing consideration of identifiable and actual "costs" of doing business--including those that might generically be referred to as "depreciation".

Although the agency has not followed the Committee's "expectation" by revising its regulations and adopting "simple schedules covering entire categories of equipment", individuals are still entitled to demonstrate "identifiable costs" of doing business. See F.S.M. § 273.11(a)(4)(i). The Department need not be bound by any amounts claimed by the petitioner as "depreciation" on their IRS tax returns. However, to the extent the petitioner can identify and substantiate specific decreases in the value of her property

and equipment through wear, deterioration, or obsolescence, she is entitled under the food stamp statute to have this included as a cost of producing self-employment income and to offset this amount from her countable income.

For the above reasons, the matter is remanded to the department to allow the petitioner to demonstrate these actual costs. The level of proof and verification necessary is a matter left to the Department to determine, subject, of course, to the petitioner's right of appeal.

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